PROMOTING FAIR AND CONSISTENT LEGISLATIVE POLICY FOR PUBLIC RETIREES

A Report to the Governor and 53rd Legislature

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A Report to the
Governor and 53rd Legislature
From the Joint Interim
Subcommittee on Public Employee Retirement Systems

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PREFACE

Origin and Purpose of Study

The growing number of retirement bills introduced each legislative session and the existence of several statewide public retirement systems has raised concerns about the Legislature's ability to make informed and well-considered decisions on complex retirement issues. Responding to this concern, particularly among legislators and retirement system administrators, the 52nd Legislature passed a joint resolution (House Joint Resolution No. 50) creating a joint interim subcommittee to study the public employee retirement systems. The resolution directed that the study include:

> (1) a comparison of the benefits provided by each retirement system and the interrelationships between and among the systems and recommendations for benefit changes to keep each system current with the needs of its members;
> (2) a study of each system's actuarial reports in order to outline the funding obligations of the state for each retirement system and to determine the progress of each system toward meeting the state's long-term obligations;
> (3) legislative options available to ensure that the current funding and administration of the benefits of the retirement systems are adequate to guarantee that present and future obligations of the systems are met in the most equitable and cost-effective manner possible; and
> (4) recommendations, including recodification, for clarifying the statutory provisions of each retirement system.

The study was funded by $30,000 from the investment earnings of the various retirement system trust funds.

Subcommittee Activity

The Joint Interim Subcommittee on Public Employee Retirement Systems (Subcommittee) conducted eight meetings and a public hearing. The Subcommittee also contracted the actuarial services of Hendrickson, Miller & Associates, Inc., to provide data on various types of cost-of-living adjustments (COLAs) for public retirees.

EXECUTIVE SUMMARY OF RECOMMENDATIONS

1. Create a joint permanent statutory retirement committee to review and propose retirement legislation. (See LC182 at Appendix A.)

A permanent statutory retirement committee should review legislative proposals from the retirement boards and employee and retiree groups at least 45 days prior to each legislative session or as necessary during a session. The permanent committee should attach to each introduced retirement bill a report on the bill's fiscal and policy implications and the committee's recommendation. This review process will not prevent the introduction of or action on retirement legislation that has not been reviewed but will provide the opportunity: (1) for a thorough hearing of retirement proposals; (2) to ensure that retirement proposals are complete and well-coordinated prior to introduction; and (3) for legislators to design consistent policy that is fair to all members of the separate retirement systems. The permanent committee will also recommend legislation to keep the retirement systems consistent, fair, current with membership needs, and responsibly funded.

The combined assets of Montana's public retirement systems (not including local plans) are $2.3 billion, with $3.7 billion in total liabilities and $977 million in unfunded liabilities.* There are approximately 46,000 active plan participants and more than 18,000 retirees and beneficiaries. The Legislature is entrusted with establishing sound, equitable, and consistent policy to ensure that these systems remain soundly funded and are able to provide public employees with financial security in retirement. A permanent

* Data taken from actuarial and financial reports prepared for the Public Employees' and Teachers' Retirement Divisions.

statutory retirement committee will assist the Legislature in discharging this duty.

2. Designate a single standing committee in each house to initially consider all retirement legislation.

The 53rd Legislature (and all subsequent legislatures) should establish rules requiring that all retirement legislation be initially referred to a single standing committee in each house to ensure that all retirement bills are considered in a coordinated manner by legislators who understand the intricacies of retirement issues. The standing committees designated to consider all retirement bills should be named accordingly. For example, the House Committee on State Administration could become the House Committee on State Administration *and Retirement*. After the retirement bills are reviewed by the designated standing committee, the bills may still be segregated and rereferred to other committees if necessary.

3. Publish a Legislator's guide to Montana's public retirement systems.

The Subcommittee has published a retirement system guide for the 1993 Legislature and recommends that the guide be updated biennially to provide easy reference to the basic structure, benefits, and funding status of each of Montana's statewide public employee retirement systems. Montana's Public Employee Retirement Systems: A Legislator's Guide, 1993, is available at the Montana Legislative Council. The permanent statutory retirement committee (discussed under the Subcommittee's first recommendation) should be responsible for preparing and updating the guide.

CHAPTER 1
LEGISLATIVE POLICYMAKING

Issue Summary

Since 1981, an average of 49 retirement bills have been introduced each legislative session, only one-third of which have been agency bills. These retirement bills have repeatedly amended various components of Montana's public employee retirement systems. (See Table 1.) Furthermore, these bills are not always referred to the same standing committees to be heard and acted upon in a coordinated fashion. Standing committees in the House and Senate that have acted on retirement legislation include State Administration, Judiciary, Taxation, Business and Industry, Local Government, Labor, Education, Appropriations, and Finance and Claims.[1] One reason for this may be that proponents of certain retirement bills feel their bill will get a more favorable consideration in one committee rather than another. Critics of the current legislative decisionmaking process, which include some administrators, legislators, and retiree organizations, also argue that standing committees without the clear responsibility of acting on <u>all</u> retirement bills often defer decisions to other committees. Eventually, the House Appropriations or Senate Finance and Claims Committees are required to make retirement policy decisions based solely on cost rather than on what is sound or consistent policy design.

TABLE 1

Bills Affecting Various Aspects of the Retirement Systems

SUBJECT	1981	1983	1985	1987	1989	1991	TOTAL
Administration	11	8	9	8	7	6	49
Contributions	9	7	15	4	13	9	57
Benefits	7	13	16	9	11	13	69
Service Credits	7	5	3	7	6	9	37
Membership	5	3	4	7	0	2	21
Eligibility	4	3	4	5	3	4	23
Investments	2	1	1	1	0	1	6
General Revision	2	1	2	2	4	1	12
Taxes	0	0	3	5	6	4	18
Studies	0	1	1	0	0	1	3
Total	47	42	58	48	50	50	295

Montana statute provides for local police and firefighter pension funds and for 10 statewide retirement systems: the Public Employees', Teachers', Municipal Police Officers', Highway Patrol Officers', Sheriffs', Game Wardens', Firefighters' Unified, Volunteer Firefighters', and Judges' Retirement Systems and the University System Optional Retirement Program.* Advocates for members of each of these separate retirement plans independently and actively lobby legislators for certain benefit enhancements or provision changes. Montana's legislators are confronted with complex issues and uncoordinated proposals, which can lead to the enactment of inconsistent and inequitable retirement policy.

The problem is not confined to Montana alone. Archibald L. Patterson, in his book Public Pension Administration, argues that nearly all state and local governments have failed to define any consistent retirement policy. This failure, he argues, invites an environment of political controversy over the

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* The membership and provisions of these various plans are outlined in Montana's Public Employee Retirement Systems: A Legislator's Guide, 1993, prepared under the direction of the Joint Interim Subcommittee on Public Employee Retirement Systems and available at the Montana Legislative Council.

management of retirement money. Patterson quotes a midwestern state legislator to make his point:

> Right now we have what amounts to a porkbarrel and piecemeal approach to pension modification. We modify one system without regard for fiscal consequences. . . . This takes place in a totally political atmosphere without any regard for how the bill will be paid, by whom, and when.[2]

To address legislative decisionmaking issues, the Subcommittee asked the following questions:

(1) How can the number of retirement bills introduced each legislative session be reduced?

(2) How can the Legislature consider retirement bills in a coordinated fashion?

(3) What will assist the Legislature in enacting sound retirement policy that is consistent from session to session and that is fair to all members of the separate retirement systems?

Summary of Testimony

Tom Schneider, representing the Montana Public Employees Association (MPEA), testified that the reason so many retirement bills are introduced each session is that public employees and retirees have a lot of unmet needs. Until the Legislature addresses these needs, especially cost-of-living increases for retirees and retiree health insurance benefits, Mr. Schneider said, numerous retirement bills will continue to be introduced.[3]

Alton Hendrickson, actuary for the Public Employees' Retirement Board, testified that, in his opinion, the Legislature considers retirement bills in a disjointed and haphazard manner, resulting in poor retirement policy that has affected the stability and fairness of the retirement systems. As one example, Mr. Hendrickson referred to a bill enacted by the 1991 Legislature that allows police officers to retire after 20 years of service regardless of age. Mr. Hendrickson suggested that the Legislature adopt overall policy guidelines against which all retirement legislation would be measured.[4]

Larry Nachtsheim, Administrator of Montana's Public Employees' Retirement Division (PERD) and President of the National Association of Retirement System Administrators, emphasized the need for a comprehensive legislative policy statement and for standard procedures to be followed when considering all retirement legislation. Mr. Nachtsheim felt that this was the best way to coordinate retirement legislation, reduce the number of retirement bills, and ensure the enactment of consistent and equitable retirement legislation. Mr. Nachtsheim proposed the following standard procedures: (1) initially refer all retirement legislation to one standing committee in each house; (2) segregate the bills for rereferral, if necessary, with all bills requiring funding being rereferred to the House Appropriations or Senate Finance and Claims Committee; and (3) establish a new, more appropriate format for fiscal notes on retirement legislation so that the full fiscal implications, including long-term effects, of a retirement bill can be understood.[5]

The concept of having all retirement legislation initially referred to one standing committee in each house and of having some type of review process for retirement legislation prior to a regular legislative session was supported by representatives of the Association of Montana Retired Public Employees (AMPRE), the Montana Education Association (MEA), MPEA, and the retirement system boards. Nevertheless, some of those who testified expressed concern that the review process not become just another bureaucratic exercise designed to prevent the legitimate interests of current and future retirees from being heard. On the other hand, Subcommittee members expressed concern that the review process not result in a legislative committee becoming simply an advocacy group for special retirement interests.[6]

Research Reports

A study of other states' approaches to the issue of how to enact consistent and equitable retirement policy revealed that in 1990, 22 of 50 states utilized some type of legislative pension oversight commission with varying powers and duties designed to assist in the legislative policymaking process. Several other states were actively considering the creation of permanent retirement committees.[7]

The Subcommittee studied the structure and authority of pension oversight commissions in six states (South Dakota, Wisconsin, Minnesota, North Dakota, Washington, and Nevada), which represent a cross section of the different ways pension oversight commissions have been organized and how they have operated.

South Dakota has both standing House and Senate Retirement Laws Committees and a permanent statutory Joint Interim Retirement Laws Committee. The statutory committee makes a continuing study of the pension, annuity, and benefit laws that relate to employees and public officers. The statutory committee generally meets only once or twice during the interim to review retirement proposals that may be introduced as bills during the regular legislative session. The standing Retirement Laws Committees of each house are assigned all introduced retirement bills.[8]

Wisconsin has a statutory Joint Survey Committee on Retirement Systems that consists of both legislative and nonlegislative members. This Joint Survey Committee reviews and reports on all retirement bills introduced in the Legislature. Although not a purely legislative committee, it has the authority to kill a bill. When a retirement bill is reported out of the Committee, the Committee's report and recommendations accompany the bill throughout the legislative process.[9]

Minnesota's Legislative Commission on Pensions and Retirement functions as a standing committee, reviewing all pension legislation introduced in the House or Senate during a legislative session. The Commission has a joint membership and can kill a retirement bill or report it out of committee with recommendations. The Commission also prepares a biennial report to the Legislature. By law, the report must contain a summary of all pension legislation passed during the previous biennium, a statement of pension policy goals and principles, and data on the fiscal status of the state's major statewide plans and local funds. The Commission meets year-round at the call of the presiding officer.[10]

North Dakota utilizes a permanent interim committee called the Employee Benefits Programs Committee to consider and review all legislation affecting the public employee retirement systems, state health insurance plans, and retiree health insurance programs. The Committee generally meets only during the interim but, by statute, must review and report on all retirement legislation prior to introduction during a legislative session.[11]

Washington's Joint Committee on Pension Policy is a permanent interim advisory committee charged with developing and recommending pension policy and funding standards. While there is no statutory requirement that retirement bills be reviewed by the Committee, a bill that has not first been reviewed rarely survives the legislative process.[12]

Nevada's Interim Retirement Committee is an advisory body that has no statutory authority other than to oversee the administration of the retirement systems and to set the salaries of various administrative officers.[13]

Subcommittee Recommendations

Subcommittee members concluded that the Legislature needs a process to ensure the enactment of fair and consistent retirement policy. To achieve this objective, the Subcommittee formulated the following unanimous recommendations.

1. ***A joint permanent statutory retirement committee should be created to review, prior to each regular legislative session, proposals amending the retirement systems. (See LC182, at Appendix A.)***

The Subcommittee unanimously agreed that the proposed statutory retirement committee should consist of both House and Senate members who must be appointed on a bipartisan basis for 2-year terms; should include at least two members of each house that serve on that house's standing committee that is regularly assigned retirement bills; and should include one Senate member from the Senate Finance and Claims Committee and one House member from the House Appropriations Committee. The Subcommittee believes that the membership outlined above is necessary to ensure that retirement legislation is considered in a bipartisan atmosphere by legislators representing standing committees that regularly consider retirement issues as well as standing committees that must approve the funding for the retirement plans in balance with the state's other fiscal responsibilities.

In addition, the Subcommittee recommends that the statutory retirement committee have the power to review retirement proposals at least 45 days prior to each regular legislative session and to attach to any introduced retirement bill a committee report on the bill's fiscal and policy implications along with the committee's recommendation on whether the bill should be enacted. The statutory retirement committee should also develop legislation and review the fiscal soundness of the retirement systems and the benefit needs of current and future public retirees.

The recommended statutory retirement committee will act to: (1) coordinate various legislative proposals affecting the retirement systems; (2) ensure that proposals are complete and responsibly funded prior to introduction in the regular legislative session; (3) provide a forum for the fair and thorough hearing of arguments for or against the proposals; and (4) apply consistent standards of good policy design. The Legislature will also benefit from the expertise that a permanent retirement committee will offer.

2. ***The leadership of the House of Representatives and the Senate should designate one of the standing committees in each house as a retirement committee with the responsibility to initially review <u>all</u> retirement legislation introduced during a legislative session.***

Initially referring all retirement legislation to a designated and appropriately named standing committee on retirement (for example, the House or Senate Committee on State Administration *<u>and Retirement</u>*) will help ensure that retirement bills are considered in a consistent, coordinated, and fair manner.

3. ***A legislator's guide to Montana's public employee retirement systems should be published biennially. (See <u>Montana's Public Retirement Systems: A Legislator's Guide, 1993</u>, prepared under the direction of the Joint Subcommittee on Public Employee Retirement Systems and published by the Montana Legislative Council.)***

The legislator's guide to the retirement systems provides an "at-a-glance" reference to the basic benefit structures and funding status of Montana's retirement systems. Additionally, the guide summarizes retirement issues and provides decisionmaking guidelines. The Subcommittee believes the guide will help legislators establish informed, equitable, and consistent retirement policy.

CHAPTER 2
POSTRETIREMENT COST-OF-LIVING ADJUSTMENTS

Issue Summary

Postretirement COLAs surfaced as the preeminent benefits issue raised in public testimony before the Subcommittee. While the Legislature has, from time to time, provided public retirees with postretirement benefit increases, these *ad hoc* increases have failed to adequately address a mounting problem. *Ad hoc* increases are seemingly expedient in the short term, but are very expensive in the long term because they are not prefunded by employee or employer contributions.

Montana statutes provide limited automatic postretirement adjustments to retirees. The Public Employees', Teachers', Game Wardens', and Sheriffs' Retirement Systems provide automatic annual postretirement increases based on a portion of the systems' investment earnings above 8%. Members of the Municipal Police Officers', Highway Patrol Officers', Firefighters' Unified, and Judges' Retirement Systems receive a minimum retirement benefit based on the salary of newly hired employees. (See Table 2.) Postretirement adjustments in three of the systems are funded by special revenue (insurance premium taxes and vehicle registration fees). However, these statutorily provided adjustments are not tied to cost-of-living or inflation indexes and vary dramatically by retirement system. In 1991, benefit increases ranged from an average of 0.84% of salary for retired game wardens to an average of 18.06% of salary for highway patrol officers.

TABLE 2
POSTRETIREMENT ADJUSTMENTS TO MONTANA'S PUBLIC RETIREMENT SYSTEMS

METHOD GIVEN	SYSTEM(S) COVERED	AVERAGE INCREASE PAID 1/1/92
(1) Retirees are paid an additional monthly retirement adjustment based on the system's investment earnings above 8%, which is the average yield assumed by the actuary.	Public Employees' Teachers' Sheriffs' Game Wardens'	\$7.03/month (1.67%) \$10.04/month (1.55%) \$22.72/month (4.09%) \$8.59/month (0.84%)
(2) Retirees are paid a minimum benefit that is equal to 1/2 the salary of a newly confirmed member. This adjustment is funded by annual payments from the state's insurance premium tax fund.	Municipal Police Officers' Firefighters' Unified	Maximum benefit varies by city and individual retiree
(3) Retirees are paid a minimum benefit by changing the basic formula to reflect the current salary of a probationary patrol officer. Also, pre-7/1/91 retirees receive an annual lump-sum supplement funded by an additional 25-cent vehicle registration fee.	Highway Patrol Officers'	Minimum benefit varies by individual retiree; supplemental benefit for pre-7/1/91 retirees in FY92 was \$1,937 (an 18.06% average increase)
(4) Retiree benefit allowances are increased based on the current salary paid to the office from which the member retired.	Judges'	Received approximately a 4% increase every 6 months beginning 7/1/91 to 7/1/93 based on salary increases for active judges

Summary of Testimony

Mr. Alton Hendrickson, Executive Director of the Hendrickson, Miller & Associates, Inc. actuarial firm and a long-time actuarial consultant for Montana's public employee retirement systems, testified in favor of providing automatic postretirement COLAs to Montana's public retirees. He strongly encouraged the Legislature to enact measures that would provide for prefunding postretirement benefit increases. He pointed out that the longer the Legislature delays in implementing prefunded adjustments, the more expensive the adjustments will become as the number of public retirees increases. Additionally, Mr. Hendrickson felt that because inflation affects all retirees equally, members of the separate retirement systems should be treated equally and receive equal postretirement benefit increases. Mr. Hendrickson observed that members of the Public Employees' and Teachers' Retirement Systems receive lower postretirement benefit increases than members of the other systems because postretirement increases are less expensive in smaller systems. He also explained that using investment earnings above 8% to fund postretirement adjustments in four of the retirement systems represents a short-term solution at best because investment earnings will soon drop below 8%. Sound actuarial funding of the retirement systems is based on investments yielding an <u>average</u> of 8% annually. By spending the earnings above 8%, the state has allowed no room for earnings to fall below 8%. The retirement systems will eventually incur a real debt for which someone will have to pay.[14]

Larry Nachtsheim, Administrator of PERD, reported to the Subcommittee that the problem with current postretirement adjustments is the lack of uniformity and equity. Mr. Nachtsheim explained that in every regular legislative session from 1973 to 1989, some form of an *ad hoc* adjustment was granted for at least one system administered by PERD. These adjustments have been provided in various forms, such as flat percentages, one-half the consumer price index (CPI) since the date of retirement, and the average 2-year increase in the CPI.

Mr. Nachtsheim recommended that postretirement adjustments be granted to public employees under the following guidelines:

(1) all retirees should be treated the same regardless of the system under which they are covered;

(2) available resources should be pooled and distributed for equal, across-the-board adjustments;

(3) the formula for calculating the amount of the postretirement adjustment should be the same for all systems;

(4) all systems should have the same age criteria for receiving the first adjustment;

(5) there should be a minimum waiting period after retirement before a retiree would become eligible to receive the adjustment; and

(6) no postretirement adjustment should be paid to a retiree who is actively employed in another public position covered under Title 19, MCA.[15]

David Senn, Executive Director of the Teachers' Retirement System, also testified in support of automatic cost-of-living adjustments for retirees. Mr. Senn explained that the Teachers' Retirement System has experienced nine *ad hoc* COLAs since 1969, none of which has approached the real increase in the cost of living.[16] Mr. Senn also reported the following research on postretirement adjustments taken from a 1990-91 survey of state and local public employee retirement systems conducted by the Public Pension Coordinating Council.[17]

74% of 201 respondents offered a postretirement adjustment, of which:

- 33% provided a fixed rate adjustment ranging from 1% to 5% annually;
- 25% provided a variable rate adjustment based on CPI;
- 9% provided adjustments through *ad hoc* legislative action; and
- 7% based adjustments on other factors such as investment earnings or a combination of fixed, variable, or *ad hoc* adjustments.

Mr. Senn also reported that the average postretirement adjustment was 3.63% annually but varied by region and occupation:

Region		Occupation	
Northeast	5.05%	General	3.37%
Midwest	3.38%	Teachers	3.46%
South	3.85%	Police/Fire	3.95%
West	3.35%	Other	4.21%

Representatives of MPEA, MEA, the MEA Retired Members Association, Retired Teachers' Association, AMPRE, the Sheriff's and Peace Officers Association, and University System faculty testified that getting the Legislature to enact meaningful postretirement COLAs or Guaranteed Annual Benefit Adjustments (GABAs) will be the top priority for these groups during the 1993 Legislative Session.[18]

Research Reports

A Legislative Council staff research paper presented to the Subcommittee summarized automatic and *ad hoc* COLAs. Automatic adjustments provide for the postretirement benefit increases to be prefunded through the retirement plan, while *ad hoc* adjustments require separate legislative appropriations.

Automatic adjustments are statutorily provided for and have proved to be extremely costly if certain control measures are not applied. For example, a COLA tied to the CPI may be capped at 3%.[19]

A recent survey showed that all but one of the 50 states--Wisconsin--provide some type of COLA for public retirees. Thirty-six percent offer a COLA tied to the CPI; 42% provide *ad hoc* COLAs; and 20% offer a fixed percentage automatic COLA or some other form of a COLA, such as an increase based on investment earnings.[20]

Consultant's Report

In response to the deep concern about and wide support for postretirement benefit increases, the Subcommittee contracted the actuarial services of Alton Hendrickson of Hendrickson, Miller & Associates, Inc. Mr. Hendrickson was asked to provide cost estimates and other fiscal data on providing postretirement benefit adjustments to Montana's public retirees.

On March 24, 1992, Mr. Hendrickson reported to the Subcommittee the cost of 2% and 4% annual benefit adjustments based on a percentage of salary for members of the Public Employees', Teachers', Game Wardens', Sheriffs', Municipal Police Officers', Firefighters' Unified, and Highway Patrol Officers' Retirement Systems. Mr. Hendrickson also presented a formula for providing the increases based on the CPI.[21] (See Mr. Hendrickson's report at Appendix B.)

The Subcommittee later asked Mr. Hendrickson to provide additional data for all the retirement systems for: (1) a flat dollar COLA based on years of service only; (2) a 1%, 2%, 3%, 4%, and 5% automatic COLA; (3) a COLA tied to the urban CPI with a 5% cap; (4) a COLA with a 2-year waiting period; and (5) a COLA paid when retirees reach ages 62 and 65. (See Appendix B.)

General Conclusions

Mr. Hendrickson reached the following general conclusions:

- A COLA based on a flat dollar amount for each year of service, thought to be an easy and equitable way to provide a COLA, is more complex than originally perceived. The dollar amount would continually have to be readjusted by the Legislature to compensate for inflation.

- The minimum benefit provided for members of the Highway Patrol Officers', Firefighters' Unified, Municipal Police Officers', and Judges' Retirement Systems is superior to a reasonable COLA that could be provided to the other systems. Thus, consideration of an automatic COLA should focus on the Public Employees', Teachers', Game Wardens', and Sheriffs' Retirement Systems, which rely solely on investment earnings above 8% for postretirement adjustments.

- A COLA tied to the CPI is complex and difficult to consistently and adequately fund because it is variable and there are disagreements about what the CPI really represents and which CPI should be used.

- A flat-percentage, automatic COLA (such as 3%) is the most effective way of providing a postretirement increase. The 53rd Legislature should provide for the prefunding of the postretirement adjustments through employee and employer contributions.[22]

Subcommittee Discussion

Motions by Senator Bianchi and Representative Cocchiarella to work toward a Subcommittee recommendation on postretirement benefit adjustments failed on tied votes.

Some Subcommittee members argued in favor of studying the issue further and in favor of a recommendation acknowledging the need to address the COLA issue.

Other Subcommittee members argued that the state was facing a fiscal crisis, that local governments would also be facing a great burden if asked to fund COLAs for their public retirees, and that it would be irresponsible and unrealistic for the Subcommittee to recommend providing postretirement benefit increases that the state cannot afford at this time. Some members argued that the issue could best be handled by the permanent statutory retirement committee that the Subcommittee is recommending.[23]

CHAPTER 3
BENEFITS, FISCAL TRENDS, AND FUNDING OBLIGATIONS

House Joint Resolution No. 50 directed the Joint Interim Subcommittee on Public Employee Retirement Systems to study the benefit structures, fiscal trends, and funding obligations of the retirement systems. Tables 3 through 11 on the following pages show the basic benefit structures and funding status of Montana's statewide retirement systems. These tables are also provided in a Legislator's guide prepared under the supervision of the Subcommittee and published by the Montana Legislative Council.[24] The tables show that:

- minimum service and age eligibility requirements for normal retirement benefits vary by system (Table 3);

- the Municipal Police Officers', Firefighters' Unified, and Highway Patrol Officers' Retirement Systems are not covered by social security (Table 5), and employer contributions to these systems are significantly higher than are contributions to systems for employees covered by social security (Table 7);

- the Firefighters' Unified, Highway Patrol Officers', and Municipal Police Officers' Retirement Systems are the most expensive systems to fund (Table 7);

- the Firefighters' Unified Retirement System has the largest unfunded liability as a percentage of payroll, with 20.98% of its total contributions being used to amortize the system's unfunded liability (Table 6);

- five of the eight systems shown in Table 7 rely on special revenue to fund retirement benefits; and

- in the Judges' Retirement System, although 41.15% of total contributions is actuarially required to fund benefits as they accrue, a 12.51% shortfall in District Court fees resulted in actual contributions of 39%, which is 2.15% short of funding promised benefits and 6.86% short of funding the system's unfunded liabilities (Table 6).

TABLE 3
PLAN FEATURES AND BASIC BENEFIT FORMULA

MONTANA'S PUBLIC RETIREMENT SYSTEMS
(As of July 1, 1992)

	PERS	TRS	SHERIFFS'	MUNICIPAL POLICE	FIREFIGHTERS' UNIFIED	HIGHWAY PATROL	GAME WARDENS'	JUDGES'
Minimum service and age required for the normal (unreduced) retirement benefit	30 yrs service, any age or 5 yrs srvc and age 60 or age 65	25 yrs service, any age or 5 yrs srvc and age 60	Pre-7/1/89 hires: 24 yrs service, any age Post-7/1/89 hires: 24 yrs srvc and age 50	20 yrs service, any age	10 yrs service and age 50	Pre-7/1/85 hires: 20 yrs service, any age Post-7/1/85 hires: 20 yrs service and age 50	20 yrs service and age 50	5 yrs service and age 65
Minimum service requirement before being vested	5 years	5 years	15 years	10 years	10 years	5 years	20 years	5 years
Provides for voluntary pro-rated early retirement benefit	Yes	Yes	Yes	No	No	Yes	No	No
Vested member may defer benefit until a later date	Yes Earliest: age 50	Yes Earliest: age 50	Yes Earliest: age 50	Yes Earliest: age 50	Yes Earliest: age 50	Yes any age	No	Yes Earliest: age 65
Basic service retirement benefit formula	1.785% x FC[1] x years of service	1.67% x FC x years of service	2.0834% x FC x years of service to 24 + 1.35% x years of service over 24 to maximum of 60% FC	2.5% x FAS[2] x years of service to 20 + 1% x FAS x years of service over 20 to maximum of 60% FAS	Pre-7/1/81 hires 2.5% x FMC[3] x years of service to 20 + 1% x FMC x years of service over 20 years of service to maximum of 60% FMC; Post-7/1/81 hires 2% x FAS x years of service to maximum of 60% FAS	2.5% x FC x years of service	2% x FC x years of service	3.33% x FS[4] x years of service to 15 + 1.785% x FS x years of service over 15

Source: Public Employees' Retirement Board, Teachers' Retirement Board, and Actuarial Reports

[1] FC = final compensation = average salary of the 3 highest consecutive years of service.
[2] FAS = final average salary = average salary of the last 36 consecutive months of service.
[3] FMC = final monthly compensation = monthly salary last received by member.
[4] FS = final salary = current salary paid to the position from which the member retired.

TABLE 4
DISABILITY AND DEATH BENEFITS

MONTANA'S PUBLIC RETIREMENT SYSTEMS
(As of July 1, 1992)

	PERS	TRS	SHERIFFS'	MUNICIPAL POLICE	FIREFIGHTERS' UNIFIED	HIGHWAY PATROL	GAME WARDENS'	JUDGES'
Disability benefits	New Plan: 1/56th x FC[1] x years of service; Old Plan: greater of either 90% of 1/56th x FC x years of service or 25% of FC; no separate duty-related disability benefit; must have 5 years of service	1/60th x FC x years of service or 25% of FC; no separate duty-related disability benefit; must have 5 years of service	Actuarially reduced normal retirement formula or 1/2 FC, if duty-related, plus 1% FC for each year over 20 up to 60% of FC	1/2 FAS[2] plus 1% for each year over 20 up to 60% of FAS	1/2 FMC[3] plus 1% FMC for each year over 20 up to 60% of FMC Post-7/1/81 hires: 1/2 FMC plus 2% FMC for each year over 25 up to 60% of FMC	Actuarially reduced normal retirement formula or 1/2 FC, if duty-related, plus 1% FC for each year over 20 up to 60% of FC[5]	Actuarially reduced normal retirement formula or 1/2 FC, if duty-related, plus 1% FC for each year over 20 up to 60% of FC	Actuarially reduced normal retirement formula or 1/2 FC, if duty-related, plus 1% FC for each year over 20 up to 60% of FC
Basic death benefit paid to beneficiaries of active members	1/12th FS[4] x (yrs of service or 6, whichever is less) plus member's contributions plus interest; paid to designated beneficiary	1/60th x FC x years of service or amount of member's contributions plus interest; paid to designated beneficiary	Reduced allowance based on salary and years of service at death or 1/2 FC, if duty-related	1/2 FAS paid to surviving spouse or to dependent children until age 18	1/2 FMC plus 1% FMC for each yr over 20 up to 60% of FMC; Pre-7/1/81 hires: receive 1% more for each year over 20; only to statutory beneficiaries	Reduced allowance based on salary and years of service at death or 1/2 FC, if duty-related	Reduced allowance based on salary and years of service at death or 1/2 FC, if duty-related	1/12th FS[4] x (yrs of service or 6, whichever is less) plus member's contributions plus interest; paid to designated beneficiary

[1] FC = final compensation = average salary of the 3 highest consecutive years of service.
[2] FAS = final average salary = average salary of the last 36 consecutive months of service.
[3] FMC = final monthly compensation = monthly salary last received by the member.
[4] FS = final salary = current annual salary paid to the position from which the member retired.
[5] Based on the system's basic service retirement formula.

Source: Public Employees' Retirement Board, Teachers' Retirement Board, and Actuarial Reports

TABLE 5
AVERAGE RETIREE PROFILES

MONTANA'S PUBLIC RETIREMENT SYSTEMS
(As of July 1, 1992)

	PERS	TRS	SHERIFFS'	MUNICIPAL POLICE	FIREFIGHTERS' UNIFIED	HIGHWAY PATROL	GAME WARDENS'	JUDGES'
Average retirement age	61 years	57 years	61 years	49 years	50 years	51 years	57 years	64 years
Average years of service at retirement	18.4 years	26 years	22 years	21.5 years	24.7 years	24.2 years	28.1 years	16.7 years
Average annual salary of active members[1]	$19,952	$29,706	$26,273	$25,171	$25,912	$27,464	$28,346	$62,474
Average monthly benefit (All retirees)	$456/month	$745/month	$690/month	$1,031/month	$997/month	$951/month	$1,151/month	$1,605/month
Average benefit as a percent of salary at retirement (1992 retirees)	32.86%	43.33%	45.83%	51.5%	54.7%	60.05%	56.2%	53%
Social security coverage	Yes	Yes	Yes	No	No	No	Yes	Yes

[1] Active members are employees currently working and contributing to the system.

Source: Public Employees' Retirement Board, Teachers' Retirement Board, and Actuarial Reports

TABLE 6
ACTUARIALLY REQUIRED FUNDING TO KEEP SYSTEMS SOUND

MONTANA'S PUBLIC RETIREMENT SYSTEMS
(As of July 1, 1992)

	PERS	TRS	SHERIFFS'	MUNICIPAL POLICE	FIREFIGHTERS' UNIFIED	HIGHWAY PATROL	GAME WARDENS'	JUDGES'
Total actively contributing members[1]	27,473	16,643	521	453	420	203	87	43
Total actuarial cost as a percentage of salary	13.4%	14.503%	14.37%	48.2%[2]	42.29%[2]	45.28%[2]	23.05%	48.01%[3]
Percentage of salary required to fund accruing benefits, i.e., normal cost	10.24%	9.876%	14.37%	23.35%	21.31%	27.31%	16.04%	41.15%
Percentage of salary used to amortize existing unfunded liabilities	3.14%	4.627%	0	14.85%	20.98%	17.97%	7.01%	6.86%
Unfunded liability or past service debt	$277,096,522	$579,400,000[4]	0	$35,350,743	$56,448,547	$23,736,147	$682,606	$4,183,758
Years required to amortize current debt	18.25 years	34.9 years	0	24.71 years	30.36 years	28.8 years	4.06 years	27.32 years[5]

Source: Public Employees' Retirement Board, Teachers' Retirement Board, and Actuarial Reports

1 Active members are employees currently working and contributing to the system.
2 Does not include special funding used to pay supplemental or minimum benefits.
3 Actual contributions to the JRS are <u>less</u> than the 48.01% required. By law, 34.71% is to be contributed from District Court fees. However, actual contributions from District Court fees (as shown on Table 5) are 22.2%, which is 12.51% short of required funding.
4 Of this amount, $30.5 million will be paid by 4.503% of the salaries of participants in the University System Optional Retirement Program.
5 This is the amortization period if the statutorily required contributions were to be made in the future; however, this will not happen without a change in funding sources.

TABLE 7
FY1992 ACTUAL FUNDING

MONTANA'S PUBLIC RETIREMENT SYSTEMS
(As of July 1, 1992)

	PERS	TRS	SHERIFFS'	MUNICIPAL POLICE	FIREFIGHTERS' UNIFIED	HIGHWAY PATROL	GAME WARDENS'	JUDGES'
Total annual payroll covered	$548,152,580	$425,125,229	$13,688,154	$11,402,679	$10,883,033	$5,575,233	$2,466,111	$2,686,371
Employer contribution	6.55%1	7.459%	7.67%	13.92%	13.02%	36.28%	7.15%	6.0%
Employee contribution	6.55%[1]	7.044%	7.00%	6%/7.2%/8.7% depending on hire date	6.0%	9.0%	7.90%	7.0%
Additional funding from other sources as a percentage of payroll[2]	None	None	None	Insurance premium taxes: 15.66% (for basic benefits) 10.66% (for supplemental benefits)	Fire insurance premium taxes: 23.27% (for basic benefits) 9.31% (for supplemental benefits)	Vehicle registration fees: 4.62% (for lump-sum supplemental benefits)	Fines and forfeitures: 10.1%	District Court fees: 22.2%[3] Supreme Court fees: 3.8%
Percentage of payroll used to fund normal costs	10.24%	9.876%	14.37%	23.35%	21.31%	27.31%	16.04%	39%[4]
Percentage of payroll to unfunded liabilities	3.14% (3.18% on 7/1/93)	4.627%	0	14.85%	20.98%	17.97%	7.01%	0[5]
Total actual FY cost as a percentage of total payroll counting all funding	13.1% (13.4% on 7/1/93)	14.503%	14.67%	48%	51.6%	49.9%	25.15%	39%

1 Increasing to 6.7% on 7/1/93.
2 Does not include the 2.5% benefit adjustment paid from the general fund to each system as required by Ch. 823, L. 1991.
3 This is 2.15% of payroll less than the 34.71% District Court fee contribution required by statute.
4 This is 12.51% of payroll less than the 48.01% required to pay for the normal cost of benefits and to amortize the debt as shown on Table 4.
5 Because total actual contributions (39%) do not cover even the normal cost of the system (41.15%), no funds are left to make payments on the unfunded liability.

Source: Public Employees' Retirement Board, Teachers' Retirement Board, and Actuarial Reports

TABLE 8

VOLUNTEER FIREFIGHTERS' COMPENSATION ACT

(As of July 1, 1992)

PENSION PLAN FEATURES	VOLUNTEER FIREFIGHTERS' PENSION FUND
Minimum service and age for normal (unreduced) retirement	20 years of service and age 55
Vested	After 10 years of service
Basic benefit formula	$120 per month for 20 years of service (prorated for 10 years through 19 years of service)
Disability	If injured in line of duty, fund pays for necessary and reasonable medical expenses, not to exceed $25,000 within 36 months of injury
Death benefit	Actual funeral expenses (only if killed in the line of duty), not to exceed $1,500, are paid to funeral provider; member's entitlement, not to exceed a total of $4,000, is paid to surviving spouse or children until spouse remarries or children reach 18 years of age
Membership	517 retirees; 4 survivors
Contributions	Funded entirely by insurance premium taxes
FY 1991 through FY 1993 benefit	$120 per month for 20 years of service
Total benefits paid in FY 1992	$699,557

TABLE 9

UNIVERSITY SYSTEM OPTIONAL RETIREMENT PROGRAM
(As of July 1, 1992)

PROGRAM FEATURES	UNIVERSITY SYSTEM OPTIONAL RETIREMENT PROGRAM
Minimum service and age for normal retirement	None. Member may begin receiving benefits at any time based on the full current value of the member's accumulated annuity.
Benefit formula	As a defined contribution plan, a member's monthly annuity depends on total contributions plus investment earnings and on the income option a member selects.
Disability benefits	None, except for the member's annuity income, which can begin at any time.
Death and survivor benefits	The full current value in a member's annuity account is payable to the beneficiary before retirement. The benefit can be paid in a single sum, as an annuity income to the beneficiary for life, or as an annuity income for a fixed period of years. The annuity may also be deferred as federal law permits.
Social security coverage	Yes.
Total active members	675
Total payroll covered	$22,243,000
Employer contribution as a percentage of payroll	2.956%
Employee contribution as a percentage of salary	7.044%
University System's contribution to TRS unfunded liability	4.503%
Total contributions	14.503%

Funding Status and Fiscal Trends

Actuaries for the statewide public retirement systems have certified that all but one of Montana's eight defined benefit cost-sharing public retirement systems are actuarially sound. The actuary for the Judges' Retirement System has concluded that that system is actuarially unsound.

As indicated on Tables 6 and 7, contributions to the Judges' Retirement System are 2.15% of payroll short of funding the normal cost of benefits as they accrue. Furthermore, no funds are available to make payments on the system's unfunded liabilities. The July 1, 1992, actuarial report on the Judges' Retirement System states:

> One of the criteria for actuarial soundness is that the annual contribution be sufficient to fund the normal cost and the unfunded liability. The Judges' Retirement System provides for a contribution of 34.71% of compensation from district court fees, but the fees are insufficient to produce this contribution. Until adequate provision is made for funding the stated contribution, it is not possible to conclude that the Judges' Retirement System is actuarially sound.[25]

Between 1988 and 1991, every system moved closer to 100% funding of the system's total pension benefit obligation (PBO). (See Table 10.) The larger the percentage of funding, the stronger the retirement system. Although the Firefighters' Unified Retirement System moved the fastest toward 100% funding, it is still the weakest system with only 40.8% of its obligations funded. The Judges' Retirement System is making the slowest progress.

In addition to the Sheriffs' Retirement System, which is funding 37.2% more than its total PBO, the Game Wardens' and Public Employees' Retirement Systems are the strongest systems.

TABLE 10
PERCENTAGE OF THE PENSION BENEFIT OBLIGATION FUNDED
(As of June 30, 1991)

RETIREMENT SYSTEM	PERCENT OF PBO FUNDED	PERCENT CHANGE FY 88 to 91
Firefighters' unified	40.8%	+ 25.93%
Municipal police officers'	49.6%	+ 10.47%
Public employees'	78.3%	+ 6.9%
Game wardens'	86.9%	+ 6.23%
Highway patrol officers'	53.2%	+ 3.91%
Teachers'	57.7%	+ 2.67%
Judges'	69.5%	+ 2.21%
Sheriffs'	137.2%	- 2.28% (decrease in over funding)

Source: Montana Public Employees' Retirement Board, 1991 Annual Financial Report

Table 11 shows the total unfunded PBO as a percent of the total payroll covered by the retirement system. This data, too, is an indicator of the strength or weakness of a retirement system. The lower the unfunded PBO as a percent of total payroll, the stronger the system.

Again, the Sheriffs', Public Employees', and Game Wardens' Retirement Systems show the most strength, while the Firefighters' Unified, Highway Patrol Officers', and Municipal Police Officers' retirement systems are the weakest.

The percent change indicated shows the systems' progress toward reducing the unfunded PBO as a percent of total payroll. A negative percent change shows how much the unfunded PBO was reduced, while a positive change shows how much the unfunded PBO was increased. [Please note that the data shown in Tables 10 and 11 are as of 1991 and are currently being updated.]

TABLE 11
UNFUNDED PBO AS A PERCENTAGE OF PAYROLL
(As of June 30, 1991)

RETIREMENT SYSTEM	PERCENTAGE OF PBO UNFUNDED	PERCENT CHANGE
Game wardens'	74.6%	- 17.93%
Municipal police officers'	316.2%	- 10.95%
Public employees'	49.8%	- 8.29%
Firefighters' unified	539.6%	- 5.70%
Highway patrol officers'	476.9%	+ 17.43%
Judges'	262.6%	+ 14.87%
Teachers'	138.2%	+ 7.47%
Sheriffs'	-85.9% (system is funded beyond system cost and has no unfunded liability)	-29.95% (indicates an increase in the system's negative unfunded PBO)

Source: Montana Public Employees' Retirement Board, 1991 Annual Financial Report and Teachers' Retirement System interim 1991 report.

APPENDIX A

Subcommittee Bill To Create A Permanent Statutory Retirement Committee

__________ BILL NO. ______

INTRODUCED BY ____

BY REQUEST OF THE JOINT INTERIM SUBCOMMITTEE ON PUBLIC EMPLOYEE RETIREMENT SYSTEMS

A BILL FOR AN ACT ENTITLED: "AN ACT CREATING A STATUTORY LEGISLATIVE COMMITTEE ON PUBLIC EMPLOYEE RETIREMENT SYSTEMS; APPROPRIATING FUNDS FOR THE COMMITTEE; AND PROVIDING AN IMMEDIATE EFFECTIVE DATE."

WHEREAS, it is necessary to establish consistency in the review of retirement legislation requests in order to better understand and control the costs of such legislation; and

WHEREAS, it is necessary to establish uniform policies for approving changes of benefits, postretirement adjustments, and funding; and

WHEREAS, the establishment of a statutory legislative committee to analyze the state's public employee retirement systems on an ongoing basis and to make recommendations for legislative action would enhance the uniformity and consistency of public employee retirement legislation.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF MONTANA:

NEW SECTION. **Section 1.** Committee on public employee retirement systems -- appointment. (1) There is a committee on public employee retirement systems.

(2) The committee consists of four members of the senate appointed by the committee on committees and four members of the house of representatives appointed by the speaker of the house.

(a) No more than two of the committee members from each house may be members of the same political party.

(b) At least two committee members from each house shall serve on the standing committee to which retirement bills are regularly assigned during a regular session. One senate member shall serve on the senate finance and claims committee. One house member shall serve on the house appropriations committee.

NEW SECTION. **Section 2.** **Terms of members -- officers -- vacancies.** (1) Appointments to the committee on public employee retirement systems are for 2 years and must be made before the final adjournment of a regular legislative session. Each member of the committee shall serve until the member's term of office as a legislator ends or until the member's successor is appointed, whichever occurs first.

(2) The committee shall elect one of its members as presiding officer and another, who must be from the opposite political party, as vice presiding officer. The committee shall elect other officers it considers necessary.

(3) A vacancy that occurs when the legislature is not

in session must be filled by the selection of a member from the same house and political party by the remaining members of the committee. An appointment to the committee under this subsection is for the unexpired term of the original member.

<u>NEW SECTION.</u> **Section 3.** **Meetings -- compensation.** (1) The committee on public employee retirement systems shall meet as often as the presiding officer considers necessary during and between legislative sessions.

(2) Committee members are entitled to receive compensation and expenses as provided in 5-2-302.

<u>NEW SECTION.</u> **Section 4.** **Staff assistance.** (1) The legislative council shall provide staff assistance to the committee on public employee retirement systems. On behalf of the committee, the legislative council has the same authority of investigation and examination under 5-11-106 and the same authority to hold hearings under 5-11-107 as it has for other committees.

(2) The committee may request personnel from state agencies, political subdivisions, or the state public employee retirement systems to furnish any information and render any assistance that the committee may request.

<u>NEW SECTION.</u> **Section 5.** **Duties of committee -- committee review and report.** (1) The committee on public employee retirement systems shall:

(a) consider the fiscal soundness of the state's public employee retirement systems, based on reports from the teachers' retirement board and the public employees' retirement board, and study and evaluate the equity and benefit structure of the state's public employee retirement systems;

(b) establish principles of sound fiscal and public policy as guidelines;

(c) as necessary, develop legislation to keep the retirement systems consistent with sound policy principles;

(d) solicit and review proposed statutory changes to any of the state's public employee retirement systems;

(e) report to the legislature on each legislative proposal reviewed by the committee. The report must include but is not limited to:

(i) a summary of the fiscal implications of the proposal;

(ii) an analysis of the effect that the proposal may have on other public employee retirement systems;

(iii) an analysis of the soundness of the proposal as a matter of public policy;

(iv) any amendments proposed by the committee; and

(v) the committee's recommendation on whether the proposal should be enacted by the legislature.

(f) attach the committee's report to any proposal that the committee considered and that is or has been introduced as a bill during a legislative session; and

(g) publish, for legislators' use, an information book on the state's public employee retirement systems.

(2) A proposal subject to review under subsection (1)(d) must be submitted to the committee at least 45 days before the first day of the next regular legislative session unless this time limitation is waived by a majority vote of the committee.

NEW SECTION. **Section 6.** Appropriation. There is appropriated for the biennium ending June 30, 1995, $7,200 from the general fund to the legislative council for use by the committee on public employee retirement systems established in [section 1].

NEW SECTION. **Section 7.** Codification instruction. [Sections 1 through 5] are intended to be codified as an integral part of Title 5, and the provisions of Title 5 apply to [sections 1 through 5].

NEW SECTION. **Section 8.** Effective date. [This act] is effective on passage and approval.

-End-

APPENDIX B

Mr. Alton Hendrickson's Reports On Postretirement Cost-of-Living Adjustments

ACTUARIAL REPORT

TO

SUBCOMMITTEE ON PUBLIC EMPLOYEE RETIREMENT SYSTEMS

ON

POST RETIREMENT BENEFIT ADJUSTMENTS

Prepared by Alton P. Hendrickson, M.A.A.A.

Hendrickson, Miller & Associates, Inc.

Submitted July 10, 1992

Hendrickson, Miller
& Associates, Inc.
ACTUARIAL CONSULTANTS

Introduction

This report illustrates the cost of post-retirement adjustments to the following seven Montana public retirement systems:

- Public Employees' Retirement System
- Teachers' Retirement System
- Police Retirement - Statewide Plan
- Firefighters' Retirement System
- Highway Patrol Retirement System
- Sheriffs' Retirement System
- Game Wardens' Retirement System

Two strategies are shown. The first is a level-dollar increase based on $1 for each year of credited service. The $1 adjustment would be increased each year to help maintain its purchasing power. The second strategy is a level-percent increase each year. Five percentages have been illustrated.

The cost of the various post-retirement adjustments have been determined independent of existing adjustment provisions. If one of the illustrated adjustment provisions were to be adopted, it would need to be coordinated with current provisions. Some alternatives would be:

1. Allow current members to select either the current or the new provision.

2. Apply either the current or the new provision each year, depending on which produces the larger benefit.

3. Replace the current provision with the new one.

4. Supplement the current provision with the new one.

The amount of funds currently available to help pay for the illustrated adjustments would depend on the coordination procedure adopted.

The calculations in this report were based on the actuarial assumptions stated in the most recent actuarial valuation reports of the various systems and membership data as of July 1, 1991. The calculations reflect legislative changes as of July 1, 1991.

This valuation has been prepared in accordance with generally accepted actuarial principles and practices. Respectfully submitted,

Alton P Hendrickson

Alton P. Hendrickson
Member, American Academy
of Actuaries

Monthly Benefit Increased $1 per Year of Service

Post-Retirement Adjustment

This approach would provide automatic increases each year in the form of a level-dollar benefit increase based on service only. The amount of this increase would be $1 for each year of service credited to the retiree.

The benefit increases would be made on each July 1 to those members who had been receiving benefits for at least 1 year. The $1 would be increased each year based on the U.S. Department of Labor's price index increase for urban consumers (CPI), but limited to 5% each year.

Advantages

The goal of this level-dollar increase would be to assist retirees in maintaining the purchasing power for basic needs. The increase would not be based on the amount of the monthly benefits but rather on the years of service credited with the retirement system.

The level-dollar increase is most advantageous to the members of those systems with the smallest benefit formula and smallest salaries. As shown on the next page, members of the Public Employees' Retirement System receive the largest percentage increase.

Example of Increase

This example illustrates 2 teachers who retire after 30 years of service, one with a final average salary of $30,000 and the other with $36,000. The annual post-retirement adjustment will be $30, increased each year by the CPI (4% in this example).

	Teacher A	Teacher B
Years of Service	30	30
Final Average Salary	$30,000	$36,000
Initial Monthly Benefit	$ 1,250	$ 1,500
2nd Year Monthly Benefit	$ 1,280	$ 1,530
3rd Year Monthly Benefit	$ 1,311	$ 1,561
20th Year Monthly Benefit	$ 2,080	$ 2,330

The difference in the teachers' benefits remains constant at $250.

Monthly Benefit Increased $1 per Year of Service

Retirement System	Add'l Cost As % Of Compensation	Average Benefit Increase	First Year Contribution
Public Employees	6.7%	4.1%	$34,195,000
Teachers	6.4	3.4	27,521,000
Police Officers	13.9	2.0	1,682,000
Firefighters	14.4	2.3	1,482,000
Highway Patrol	16.0	2.7	831,000
Sheriffs	6.2	2.8	719,000
Game Wardens	9.4	2.5	223,000

Benefits Increased at A Level Percent Annually

Post-Retirement Adjustment

This approach would provide automatic increases each year in the form of a level percent of the benefit. The costs are shown at annual increases of 1%, 2%, 3%, 4%, and 5%. The reduced costs for delayed increases are also shown. The delays include a 2-year delay as well as delays until age 62 or 65.

The benefit increases would be made on each July 1 to those members who had been receiving benefits for at least 1 year. The 2-year delay would require that members be retired for at least 3 years. Increases delayed until age 62 or 65 would first be paid on the July 1 following the attainment of the required age provided the member had been retired at least 1 year.

Advantages

The biggest advantage of this level-percent increase provision would be simplicity and cost control. Because annual increases are fixed, and not tied to a variable index, the costs can be projected more accurately.

The level-percent increase is most advantageous to the members of those systems with the largest formula and salaries. The 2-year delay has a uniform impact on all systems; however, the age 62 or 65 deferral reduces benefits more on the smaller systems. These systems allow members to retire earlier which results in a longer deferral period until age 62 or 65.

Example of Increase

This example again illustrates 2 teachers who retire after 30 years of service, one with a final average salary of $30,000 and the other with $36,000, using a constant 3% annual increase.

	Teacher A	Teacher B
Years of Service	30	30
Final Average Salary	$30,000	$36,000
Initial Monthly Benefit	$ 1,250	$ 1,500
2nd Year Monthly Benefit	$ 1,288	$ 1,545
3rd Year Monthly Benefit	$ 1,326	$ 1,591
20th Year Monthly Benefit	$ 2,192	$ 2,630

By the 20th year, the difference in the teachers' benefits will have grown from $250 to $438.

Benefits Increased 1% Annually

Cost As A Percent of Annual Compensation

Retirement System	No Delay	2-Year Delay	Delay to Age 62	Delay to Age 65
Public Employees	1.77%	1.33%	1.14%	.70%
Teachers	1.90	1.43	1.23	.75
Police Officers	5.71	4.57	1.27	.79
Firefighters	5.43	4.35	1.21	.75
Highway Patrol	5.51	4.41	1.23	.76
Sheriffs	2.41	1.86	.89	.53
Game Wardens	3.97	3.06	1.47	.87

Benefits Increased 2% Annually

Cost As A Percent of Annual Compensation

Retirement System	No Delay	2-Year Delay	Delay to Age 62	Delay to Age 65
Public Employees	3.80%	2.85%	2.45%	1.49%
Teachers	4.23	3.18	2.73	1.66
Police Officers	12.68	10.16	2.82	1.76
Firefighters	12.04	9.64	2.68	1.67
Highway Patrol	12.24	9.80	2.72	1.70
Sheriffs	5.03	3.88	1.86	1.11
Game Wardens	8.48	6.53	3.14	1.87

Benefits Increased 3% Annually

Cost As A Percent of Annual Compensation

Retirement System	No Delay	2-Year Delay	Delay to Age 62	Delay to Age 65
Public Employees	6.16%	4.63%	3.98%	2.42%
Teachers	7.06	5.30	4.56	2.78
Police Officers	21.21	16.99	4.72	2.94
Firefighters	19.97	16.00	4.45	2.77
Highway Patrol	20.36	16.31	4.53	2.82
Sheriffs	8.10	6.24	3.00	1.79
Game Wardens	13.83	10.66	5.13	3.05

Benefits Increased 4% Annually

Cost As A Percent of Annual Compensation

Retirement System	No Delay	2-Year Delay	Delay to Age 62	Delay to Age 65
Public Employees	8.92%	6.70%	5.76%	3.51%
Teachers	10.47	7.86	6.76	4.12
Police Officers	31.69	25.38	7.05	4.39
Firefighters	29.41	23.56	6.55	4.08
Highway Patrol	30.24	24.22	6.73	4.19
Sheriffs	11.87	9.15	4.40	2.62
Game Wardens	20.38	15.70	7.55	4.49

Benefits Increased 5% Annually

Cost As A Percent of Annual Compensation

Retirement System	No Delay	2-Year Delay	Delay to Age 62	Delay to Age 65
Public Employees	12.15%	9.12%	7.84%	4.78%
Teachers	14.55	10.93	9.39	5.72
Police Officers	44.60	35.72	9.93	6.18
Firefighters	40.60	32.52	9.04	5.63
Highway Patrol	41.84	33.51	9.31	5.80
Sheriffs	16.60	12.79	6.15	3.66
Game Wardens	28.55	22.00	10.58	6.29

Statistical Information

Practical decisions on post-retirement adjustment provisions require information about the long-term impact of various alternatives, projections of future need based on past experience, and membership statistics which affect the ultimate cost of the increases. The following tables provide a summary of this information.

Annual Increases

This table illustrates the amount by which a $1,000 monthly benefit will increase at various rates of annual increases.

Year of Retirement	Annual Rate of Increase 2%	4%	6%
1	$1,000	$1,000	$1,000
5	1,082	1,170	1,262
10	1,195	1,423	1,689
15	1,319	1,732	2,261
20	1,457	2,107	3,026
25	1,608	2,563	4,049
30	1,776	3,119	5,418
35	1,961	3,794	7,251
40	2,165	4,616	9,704

From July 1, 1991 through June 30, 1992, the CPI increased 3.0%. For the preceding 12 months, the rate was 4.7%. During the last 10 years, the CPI has increase at an average annual rate of 3.8%. During the preceding 10 years, it averaged 8.8%.

Life Expectancies

While sex is not a factor in the benefits provided by the public retirement systems, it does impact the cost of post-retirement benefit increases. On the average females live longer than males and, as such, are expected to receive post-retirement increases over a longer period.

Another factor is the age at which members are entitled to retire with unreduced benefits. The earlier the retirement age, the longer that post-retirement benefit increases must be paid. The following table shows the life expectancy at various retirement ages by sex.

Year of Retirement	Expected Lifetime Females	Males
45	40.6	34.7
50	35.9	30.1
55	31.2	25.7
60	26.6	21.5
65	22.1	17.5
70	17.9	13.9
75	14.1	10.7

The regular monthly benefit for police officers, firefighters and the highway patrol provides a continuation of the benefit to the spouse in the event of the member's death. This feature adds approximately 10 years to the expected payout period.

Membership Averages

The membership statistics and the retirement experience of the systems determine the cost of the various post-retirement adjustments illustrated above. The following tables provide information about the average statistics for active members and those receiving benefits.

Active Membership Averages

Retirement System	Active Members	Entry Age	Attain Age	Past Service	Annual Salary
Public Employees	26,908	35.5	42.9	7.4	$18,967
Teachers	16,255	30.1	42.6	12.5	29,500
Police Officers	445	27.2	36.9	9.7	27,186
Firefighters	416	26.8	39.7	12.9	24,728
Highway Patrol	203	27.2	39.8	12.6	25,583
Sheriffs	525	31.8	39.6	7.8	22,076
Game Wardens	91	26.3	39.0	12.7	26,026
Judges	43	48.1	56.6	8.5	56,035

Retired Membership Averages

Retirement System	Retired Members	Retire Age	Attain Age	Service At Ret	Annual Benefit	Years Ret'd
Public Employees	10,429	59.8	70.6	18.0	$ 5,244	10.8
Teachers	6,673	58.0	70.2	24.7	8,700	12.2
Police Officers	429	46.3	63.8	19.1	11,496	17.5
Firefighters	396	47.9	65.7	22.2	11,460	17.8
Highway Patrol	191	48.8	64.1	23.0	10,092	15.3
Sheriffs	93	56.0	63.1	18.2	7,764	7.1
Game Wardens	59	55.9	66.1	26.4	12,540	10.2
Judges	31	61.0	75.3	17.3	19,248	14.3

Hendrickson, Miller
& Associates, Inc.
ACTUARIAL CONSULTANTS

Securities Building • 101 N. Last Chance Gulch
P.O. Box 823 • Helena, Montana 59624
Telephone 406/442-5222
FAX 406/442-5089

July 16, 1992

M. Valencia Lane
Montana Legislative Council
Legal Services Division
Room 138, State Capitol
Helena, MT 59620-1706

Re: Post-Retirement Adjustment Report

Dear Valencia:

As a supplement to the recent actuarial report, I have determined the cost of providing a 3-year deferred annual 2% increase. This increase would be granted annually to all retirees who have been retired at least 4 years on each July 1. I have shown the cost for current retirees and active members.

	Cost as a Percent of Compensation		
Retirement System	Retired Members	Active Members	All Members
Public Employees	.58%	1.87%	2.45%
Teachers	.62	2.05	2.67
Police Officers	2.93	5.80	8.73
Firefighters	3.01	5.28	8.29
Highway Patrol	2.89	5.54	8.43
Sheriffs	.43	2.90	3.33
Game Wardens	1.88	3.74	5.62

Sincerely,

Alton P Hendrickson

Alton P. Hendrickson, M.A.A.A.

Hendrickson, Miller
& Associates, Inc.
ACTUARIAL CONSULTANTS

Securities Building • 101 N. Last Chance Gulch
P.O. Box 823 • Helena, Montana 59624
Telephone 406/442-5222
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July 31, 1992

Sheri S. Heffelfinger, Researcher
Legal Services Division
Room 138, State Capitol
Helena, MT 59620-1706

Re: Post-Retirement Adjustment Report

Dear Sheri:

As requested, I have determine the additional contribution which will be required during the first year under various increase assumptions. These contributions correspond to the percentage increases illustrated for each of the retirement systems in my report of July 10. 1992.

Sincerely,

Alton

Alton P. Hendrickson, M.A.A.A.

Benefits Increased 1% Annually

Required First Year Contribution

Retirement System	No Delay	2-Year Delay	Delay to Age 62	Delay to Age 65
Public Employees	9,033,407	6,783,186	5,830,161	3,552,839
Teachers	8,170,120	6,134,943	5,272,996	3,213,308
Police Officers	690,778	553,313	153,767	95,742
Firefighters	558,582	447,424	124,340	77,420
Highway Patrol	286,151	229,207	63,697	39,661
Sheriffs	279,320	215,244	103,544	61,562
Game Wardens	94,024	72,455	34,855	20,723

Benefits Increased 2% Annually

Required First Year Contribution

Retirement System	No Delay	2-Year Delay	Delay to Age 62	Delay to Age 65
Public Employees	19,393,756	14,562,771	12,516,730	7,627,564
Teachers	18,189,268	13,658,321	11,739,354	7,153,839
Police Officers	1,533,986	1,228,723	341,465	212,610
Firefighters	1,238,551	992,079	275,701	171,663
Highway Patrol	635,660	509,164	141,498	88,102
Sheriffs	582,978	449,243	216,110	128,488
Game Wardens	200,837	154,765	74,450	44,265

Benefits Increased 3% Annually

Required First Year Contribution

Retirement System	No Delay	2-Year Delay	Delay to Age 62	Delay to Age 65
Public Employees	31,438,299	23,607,019	20,290,278	12,364,683
Teachers	30,358,447	22,796,158	19,593,342	11,939,977
Police Officers	2,565,919	2,055,301	571,173	355,636
Firefighters	2,054,307	1,645,500	457,289	284,727
Highway Patrol	1,057,356	846,942	235,367	146,550
Sheriffs	938,792	723,433	348,010	206,910
Game Wardens	327,545	252,406	121,421	72,191

Benefits Increased 4% Annually

Required First Year Contribution

Retirement System	No Delay	2-Year Delay	Delay to Age 62	Delay to Age 65
Public Employees	45,524,290	34,184,189	29,381,377	17,904,703
Teachers	45,021,663	33,806,767	29,056,981	17,707,020
Police Officers	3,833,756	3,070,838	853,394	531,359
Firefighters	3,025,397	2,423,343	673,453	419,320
Highway Patrol	1,570,454	1,257,934	349,583	217,665
Sheriffs	1,375,736	1,060,142	509,985	303,212
Game Wardens	482,672	371,947	178,927	106,381

Benefits Increased 5% Annually

Required First Year Contribution

Retirement System	No Delay	2-Year Delay	Delay to Age 62	Delay to Age 65
Public Employees	62,008,982	46,562,545	40,020,597	24,388,133
Teachers	62,565,922	46,980,751	40,380,046	24,607,177
Police Officers	5,395,567	4,321,849	1,201,053	747,826
Firefighters	4,176,509	3,345,383	929,691	578,864
Highway Patrol	2,172,877	1,740,475	483,682	301,161
Sheriffs	1,923,944	1,482,591	713,206	424,037
Game Wardens	676,168	521,055	250,655	149,027

APPENDIX C

Glossary of Common Retirement Terms

Glossary of Common Retirement Terms

Active members - Persons currently employed in positions covered by the retirement system, earning service credits, and contributing a percentage of their salary to the retirement system.

Actuarial valuation - A mathematical process used to determine the financial condition of a retirement system at a particular point in time and to project the system's future funding needs.

Annuity - Equal and fixed payments for life that are calculated to be the actuarial equivalent of a lump-sum payment. This lump sum is usually the member's accumulated contributions, plus interest. An annuity is not a service, disability, or survivorship benefit and is not adjusted by a COLA, GABA, or any other postretirement adjustment.

Benefit formula - The mathematical formula used to calculate the service or disability retirement or survivorship benefit in a defined benefit plan. This formula defines the benefit as a certain percentage of the member's salary at retirement per year of service. For example: 1/56th x salary x years of service = monthly pension.

COLA - A Cost-of-Living Adjustment. This term refers to an increase in a retiree's monthly benefit based on an increase in the cost of living.

Defined benefit plan - A retirement plan that promises certain benefits (defined by a formula) at an actuarially determined cost. The cost is expressed as a fixed percentage of active members' salaries.

Defined contribution plan - A retirement plan that provides varying annuities defined by contributions on account and a member's age and choices of payout on the day the member retires. No adjustments may be made to the monthly payout after the annuity is initiated.

GABA - A Guaranteed Annual Benefit Adjustment. This term refers to an automatic increase in a retiree's monthly benefit allowance by an amount that is specified in statute but which may not be formally connected to the cost of living.

Inactive Members - Members of the retirement system who have contributions in the system but are no longer employed in positions covered by the system. Inactive members are no longer earning service credits or contributing a portion of their salaries to the retirement system.

Normal cost - The fixed percentage of total salaries required to fund the benefits promised to members of a retirement system as the benefits accrue.

Normal retirement - The full retirement benefit that is paid when a member has completed the minimum years of service and/or attained the minimum age required to be eligible for full benefits. Although early retirement benefits are paid, sometimes on a pro-rated basis, these benefits are not considered normal retirement benefits.

Pension - A benefit paid by an employer to a retiree or survivor because of previous service performed for the employer.

Unfunded liability - That portion of the total liabilities of the system that cannot be funded by the system's current assets or the anticipated future normal contributions of members and employers plus anticipated investment earnings. Individual unfunded liabilities are created when a benefit is promised for service performed prior to the benefit's effective date when contributions are not raised sufficiently to pay the normal cost of the benefit as it will accrue.

Vested - A member of a retirement system is vested after being an active member for a certain minimum number of years. After becoming vested, a member has specified rights under the system. If a member terminates employment under a system before being vested, the member will be eligible only for a refund of the member's accumulated contributions, plus interest.

lao 2295shxa

ENDNOTES

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4. Joint Interim Subcommittee on Public Employee Retirement Systems, Minutes, Montana Legislative Council, November 6, 1991, pp. 12-13.

5. Ibid., Exhibit 4.

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11. North Dakota Century Code, Section 54-35-02.4; telephone interview with Jeff Nelson, staff researcher for the Employee Benefits Programs Committee, March 17, 1992.

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15. Joint Interim Subcommittee on Public Employee Retirement Systems, Minutes, Montana Legislative Council, March 24, 1992, Exhibit 3.

16. Ibid., Exhibit 5.

17. Joint Interim Subcommittee on Public Employee Retirement Systems, Minutes, Montana Legislative Council, March 24, 1992, Exhibit 5.

18. Joint Interim Subcommittee on Public Employee Retirement Systems, Minutes, Montana Legislative Council, February 5-6, 1992, public hearing.

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21. Joint Interim Subcommittee on Public Employee Retirement Systems, Minutes, Montana Legislative Council, March 24, 1992, pp. 2-7.

22. Joint Interim Subcommittee on Public Employee Retirement Systems, Minutes, Montana Legislative Council, May 11, 1992.

23. Joint Interim Subcommittee on Public Employee Retirement Systems, Minutes, Montana Legislative Council, August 3, 1992.

24. Sheri S. Heffelfinger, Montana's Public Employee Retirement Systems: A Legislator's Guide, 1993, Montana Legislative Council, 1992.

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